DOES P&C LOSS PREVENTION PREVENT LOSSES?

The Management Challenges of Loss Prevention in the 21st Century

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Is the mission of loss prevention crystal clear?

"How many of you here today surveyed job sites during the past year and found workplace hazards?" This was the starting question from a keynote speaker at a recent ASSE annual conference. The keynote ASSE convention speaker had 3,000 dangling hands in the air. "And how many of you reported those hazards to your client with recommendations for improvement?" Again, 3,000 forearms stretched to the sky. "And how many of you were successful in eliminating all of these hazards?" Perplexed silence with no hands waving…

Just when P&C carriers first decided to invest in accident reduction is lost to history. Today, major carriers continue to invest in "Loss Prevention" or "Loss Control". Some clients demand it and most expect it. Do insurors know if this service works? Do they understand what they had intended to get for their investment? Can they calculate a point of diminishing returns to guide them in their investment strategy? For companies large and small the answers are a resounding "No". There are no measurements to determine the relative success of Loss Control efforts. There is no data to guide the allocation of this skilled resource. Why has this occurred and what can be done about it? The answer begins with understanding the mission of loss control.

The very terms "loss prevention" or "loss control" imply that for an up front investment a reduction in paid losses will follow. You might offer to do this yourself as a hedge against losses on your investment, or you might persuade the client to undertake the effort for you. You are in a quandary. Should you continue your efforts? Some carriers never went this route. Their safety engineers were most helpful estimating expected losses from potential clients. But why worry about someone's driving ability when you have their driving record? Insurors have access to multi-year loss records. Even with a negative survey report, if the last five years have shown a good return for the risk-taker, what are you to do?

Carriers are caught up in this most basic of discussions. Do we keep our loss prevention staff? One major carrier just terminated 50% of its loss control staff. "There was no clear justification for continuing those operations," read the press release. "Then why not ditch the other 50% as well?" might be an appropriate Board response. How much investment in loss control is enough? Carriers today who cannot answer this question still fund sizeable loss control operations. CEO's and CFO's rarely understand this corporate division. Questioning the value of loss control is a premature ultimate, a questioning of an assumption so preposterous as to be unthinkable. But is there evidence that loss prevention really prevents losses?

What If You Knew It Worked and Exactly How Much?

Studies indicate loss prevention operates on budgets equal to 2-3% of earned premium. Claim operations, by contrast, run on a diet of 5-7% of premium. Budgets under 1% of premium are not uncommon. What would you do in a highly competitive market lacking the knowledge to quantify payback on an investment equal to 2% of your total revenue? To best answer this question, try turning it around. "What would you invest if you knew precisely the amount of losses your loss prevention department could prevent?" Karl Jacobson manages Liberty Mutual's loss control operations. "We have moved away from the traditional field visits made or recommendations submitted," he says. "We are focusing on direct outcome measures. Loss ratio was used, but it is impacted by price and not just loss reduction. It is a difficult challenge, but we are being persistent." Bob Drew, Loss Prevention Services Manager for the innovative Texas Workers' Compensation Insurance Fund, cuts right to the chase. "We no longer track activity measures at all," says Drew in a matter-of-fact Texas drawl. "Tracking the number of field visits made tells me how many cups of coffee we consumed, but not much more.. I need targeted data that can direct and focus our efforts to prevent losses."

Today's loss prevention budgets are influenced more by last year's budget than by any other factor. You may get a bit more or less depending on premium projections, but the critical assumption is that whoever made the first staffing decision knew what they were doing. They probably had not a clue. This leads to a striking deduction: ***Just about every loss prevention department in existence is improperly staffed.*** The budget may be too large or too small, but given that it was derived by chance, the probability of its being even close to accurate is virtually nil. The budget issue is just one effect of the problem. Consider the problems that mid-level management must face:

1. What size accounts get any service?
2. How often do you service accounts?
3. Do you charge extra for this service?
4. How much do you invest in the accounts you do service?
5. Do you service the small account at all?
6. How long do you have to make your safety efforts pay off? One year? Maybe two? Said another way, are you really trying to rehabilitate accounts for the next insuror?
7. What if the client seems is not cooperative? Should you try persuasion or exclude them immediately?
8. Can you expect your staff to be generalists or do you turn to specialization?

These are tough decisions, and they are being made in insurors' safety operations every day. But are they being made in a way that maximizes return on investment?

Does Management Have the Tools to Get the Job Done Properly?

The effects of the problem are clear. What alternatives are available to management?

1. Maintain the status quo.
2. Stop or reduce loss prevention until a proven method is found.
3. Test approaches using control group and sampling techniques.
4. Really begin to quantify both your efforts and your outcomes.

Melissa Diede manages Loss Control for SAIF Corporation, the Oregon workers' comp fund that is in the forefront of measuring loss prevention outcomes. "We worried about our consultants' reaction to a more quantified approach to field operations. Were we ever wrong! Three months after our first outcomes-based tool was rolled-out, we had field reps demanding more and better measurement tools. They could finally see what they were doing. They wanted more."

Maintaining the status quo is not a viable option, especially if competitors are choosing other, wiser approaches. The "Stop or Cut-Back" approach is frequently tried by carriers. The use of control groups and experimentation should work, but imagine the legal fallout! Only the last option promises improvement not only in loss prevention processes but also in actual outcomes. Are the tools available? Of course. They always were.

Towards a Decision That Will Solve the Problem

I am involved in research and development of systems that bring operational management directly to bear on these issues. While some of our innovations are proprietary, the essential ingredients are logical. ***(See table A.)***

LOSS CAUSE FACTOR	LOSSES 1998	LOSSES 1999	LOSSES 2000	EXP'd LOSSES 2001	AVG. COST PER LOSS	EXP'd LOSS COST 2001	LOSS GOAL 2001	EXPECTED SAVINGS 2001	ACTUAL LOSSES 2001
FALL FROM HEIGHT	8	11	6	8.33	$22,821	$190,175	5	$75,994	
SPRAIN	22	28	26	25.33	$12,808	$324,427	15	$132,307	
BURN	4	0	3	2.33	$15,234	$35,495	1	$20,261	
TOXIC EXP	12	14	18	26	$4,225	$109,850	15	$46,475	
TOTAL	46	53	53	62	$10,644	$659,947	36	$275,037	

Table A: Translating expected losses into expected savings yields ROI.

1. Predict the number and type of losses for the coming period.
2. Trend losses to reflect anticipated economic conditions.
3. Quantify losses using historical cost information.
4. Develop heuristics to guide decisions affecting service levels.
5. Prepare Action Plans that the client accepts.
6. Measure outcomes periodically.
7. Adjust heuristics based on outcome data.
8. Modify your performance and the operations of your client.
9. Improve efficiency as a means to expand service.
10. Base budgets on proven outcomes.

"It is never too late to be what you might have been." - George Elliot

Change is generally resisted in any form. Fear of the unknown. Fear of failure. Inertia. Moving loss prevention to a quantitative approach will be a wrenching experience for most carriers. Michael Billings in charge of Loss Control at *OneBeacon* Insurance Company knows about harnessing change. With corporate mergers behind him, he is busy tying together multiple mainframe systems into a single database. His plan is to have a smart system select policyholders for service based on loss prevention potential. The same system will deliver assignments to the field, upload their surveys to underwriting and even provide them with maps to speed up their field visits and assist them with improved scheduling.. "We have to find a better system to address the loss control needs of our clients," says Billings. "This can become an expensive undertaking not only for *OneBeacon*, but especially for our clients. They deserve to know the results of our safety efforts. We have to measure the savings from losses that we prevented from occurring. Not easy, but something we are going to do," says Billings. Billings is working with Advanced Management Systems of Troy, New York to implement a next-generation system that will select, assign, and measure the results of his company's loss control efforts. The elusive ROI becomes a real number -- at the individual, team, regional or company level. Will budgets get hurt in this process? Not if you believe, as I do, that loss prevention really does prevent losses. With the value of loss control operations quantified, I predict a leap in resources committed to loss prevention. This could be safety's finest hour.

About the author:

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